Thursday, June 25, 1987

IN THE UNITED STATES BANKRUPTCY COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

In re

HIGHLAND HOUSE, INC., No. 1-86-01715

Debtor.

_____/

CHARLES DUCK, Trustee,

Plaintiff,

v. A.P. No. 1-87-0001

ROGER JANIS,

Defendant.

_____/

MEMORANDUM OF DECISION

The debtor filed its Chapter 7 petition on October 24, 1986. This action by the Trustee

seeks to avoid the assignment of a note from the debtor to defendant Roger Janis on May 30, 1986. The note in question was part of the proceeds of a settlement of a lawsuit between the debtor and third parties. The testimony established that Janis met Manfred Fischer, owner of the debtor, in late 1981, and they soon became friends. The debtor's restaurant business frequently became strapped for cash, and Janis began giving Fischer short-term loans for the business in exchange by exchanging checks; Janis would hold the debtor's check until Fischer told him that there were funds in the bank to cover it. After around eight to ten of these short-term loans, Janis arranged for the debtor to obtain a series of loans from Bank of America which Janis guaranteed. Some time during this relationship, Janis became a director of the debtor. On September 11, 1984, Fischer borrowed $100,000.00 from Janis. $85,000.00 of this loan went to pay off Bank of America on the obligation Janis had guaranteed; the remaining $15,000.00 went into the debtor's business. On February 7, 1986, Fischer closed the doors of the debtor's restaurant. Janis resigned as a director on March 14, 1986. The lawsuit between the debtor and third parties was stettled on May 2, 1986. On May 30, 1986, Fischer delivered the original of a note for $15,000.00 which the debtor took from the third parties to Janis, with the intent that Janis become the owner of the note as payment for interest due to Janis on the 100,000.00 loan. The note was not endorsed or otherwise marked. At the same time, Fischer and his wife executed an assignment of the deed of trust securing the note, but signed it individually rather than in the name of the corporation. The Trustee's first argument is that the transfer of the note is avoidable as an insider preference pursuant to 11 U.S.C. section 547(b). However, the evidence did not established that Janis was an insider on the date of the transfer. While Janis had indeed been an insider for preference purposes up until March 14, 1986, the undisputed evidence was that Janis exercised no control over the debtor after that date. The testimony of both witnesses was that the decision to transfer the note to Janis was "mutual" and not the result of any control or pressure exerted by Janis. Moreover, Janis had not been consulted and played no role in the other major decisions by the debtor, including the settlement of the lawsuit, the closure of the business, and the filing of the bankruptcy petition. The definition of "insider" in the Bankruptcy Code is not exclusive; it is a flexible term to be applied on a case-by-case basis. In re Missionary Baptist Foundation, Inc. (5th Cir.1983) 712 F.2d 206. However, the person accused of being an insider must have exercised control over the debtor on the date of the transfer in order to make the transfer avoidable as an insider preference. In re Tennessee Wheel & Rubber Co. (Bkrtcy.M.D.Tenn.1986) 62 B.R. 1002, 1005. Existence of an insider relationship which terminated before the transfer is not relevant. In re Camp Rockhill (Bkrtcy. E.D.Pa.1981) 12 B.R. 829, 834. In this case, the evidence did not establish that Janis exercised sufficient control over the debtor on the date of the transfer to support a finding that he was then an insider. The Trustee's argument that the transfer was ineffective due to the defect in assignment of the note and its deed of trust is not meritorious. The evidence was clear that Fischer delivered the note to Janis with the intent to transfer all rights in it as a payment for interest due. A delivery with such intent, even without an endorsement or written assignment, is sufficient to validly transfer ownership of the note. Johnson v. All Night and Day Bank (1911) 17 Cal.App. 571. The only effect of the failure to properly endorse or assign the note is that the transferee does not have the rights of a holder in due course. 11 **Am.Jur.2d,** Bills and Notes sec. 375. The evidence not establishing an avoidable transfer, this action shall be dismissed and Janis shall recover his costs of suit. Although the Trustee did not prevail, the bringing of the action was perfectly proper and the issue was certainly close enough to allow the Trustee to proceed to trial in good faith. Accordingly, Janis' prayer for sanctions against the Trustee is denied. Counsel for Janis

shall prepare and submit a form of judgment in accordance with this decision. This memorandum shall constitute findings and conclusions pursuant to Bankruptcy Rule 7052 and FRCP 52(a).

Dated: June 25, 1987 _____

ALAN JAROSLOVSKY

U.S. BANKRUPTCY COURT
